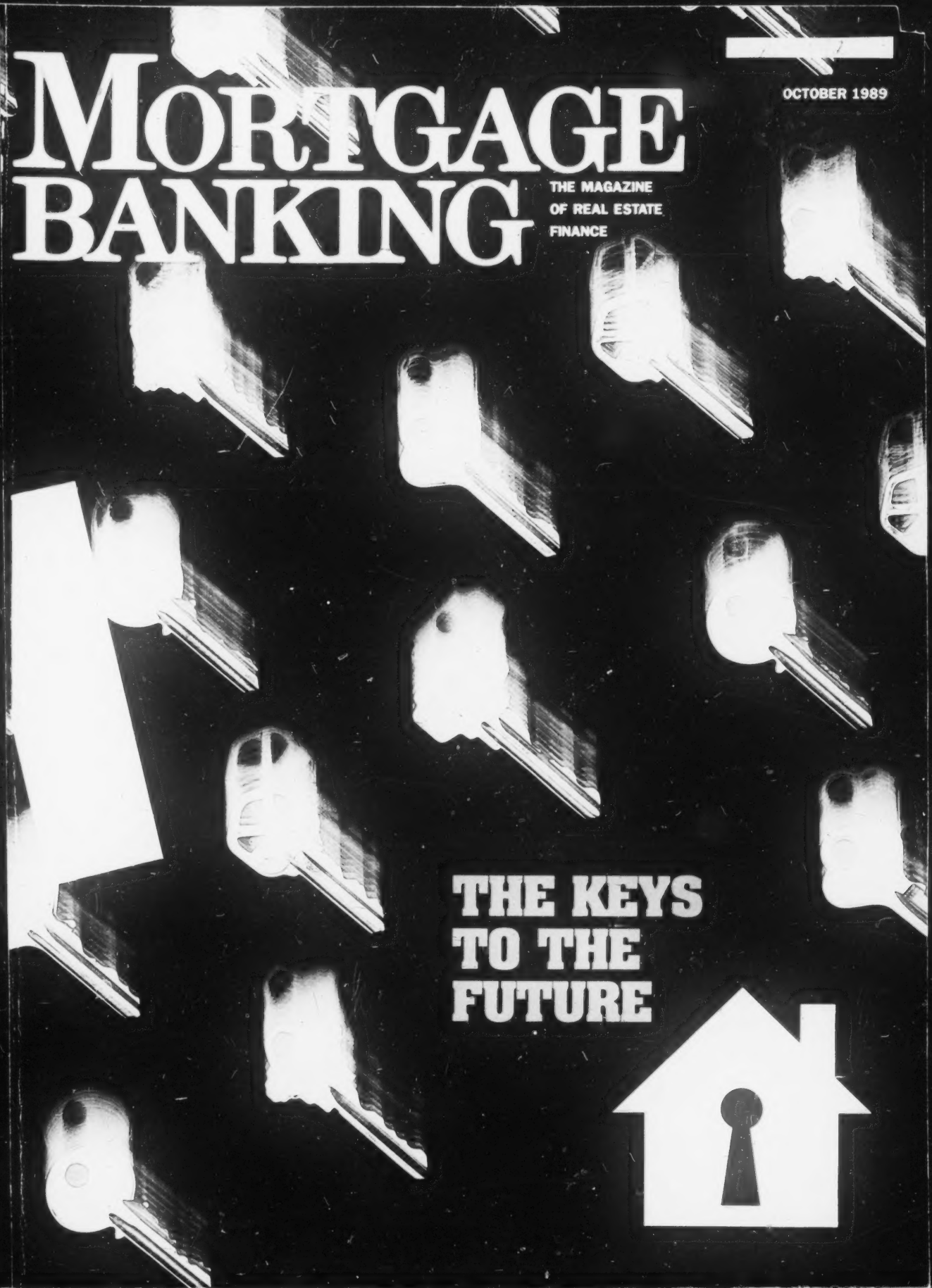
MORTGAGE BANKING

THE MAGAZINE OF REAL ESTATE FINANCE

OCTOBER 1989



THE KEYS TO THE FUTURE

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OCTOBER 1989 VOLUME 50 NUMBER 1

COVER: Keys to the Future

The future holds no simple answers. There is no single door that will open onto a field of prosperity. Instead, there are many keyholes with many keys to fit them. Each mortgage industry survivor will have to forge its own set of keys to open the now obscured doors leading to future financial success.

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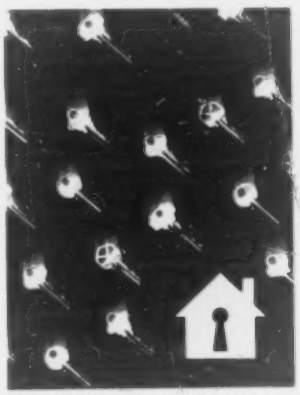
Looking through the Keyhole



This month we try to look behind some of the hidden doors through which the industry must pass before arriving at the marketplace of tomorrow. Certainly, some trapdoors exist that might bar the way for those seeking a thriving spot in the next century's housing business environment.

Demographic change is one of those trapdoors. A historic transition between a generation of record numbers—the baby boom—to one of meager numbers—the baby bust—will have a stark impact on housing values and housing demand in the not-so-distant future. The cover story explores how this much smaller generation will shape the type of housing and move-up markets that will retain demand. From our author's account we learn why this financially pragmatic generation will be very different homebuyers than their generational forebears. How this buying behavior plays out will be one key to the future.

Lenders must watch complex social, regional and economic forces, as well as internal industry innovations, to get a reading on what the future will bring. The industry is in the midst of wholesale change. And trees are hard to make out from the middle of the forest. While everyone knows that the working blueprint for the thrift industry was just radically rewritten, what we don't know is how that change will affect mortgage competition on Main Street and open-market pricing for mortgage banking's main commodity—servicing.

Some obstacles blocking the way to a future, well-housed nation can clearly be seen even from the darkness of today's forest. Housing unaffordability—a crisis of growing proportions—is readily apparent in America today. It is a complex problem—the result of a supply/demand equation severely stressed by demographic and economic forces. It is a problem too large for the nation's housing financiers to solve alone. Builders can build and consumers can earn a paycheck, but if the product cannot be priced within reach, there is no housing market working in this country. This problem will clearly still be around in tomorrow's marketplace. And the social fallout from a nation increasingly incapable of purchasing adequate shelter is one trapdoor this nation could do without.

Janet Reilley Hewitt
Editor

COMING IN NOVEMBER

Marketing Mortgage Products

It's a jungle out there. The competition is fierce. The November issue scopes out what some companies are doing to survive. We also explore how HUD survived its own long hot summer.

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Out of these turbulent times will emerge a changed industry. What will it look like?

Toward the Year 2000

Warren Lasko

As we peer over the threshold at the 21st century, the business of financing real estate is in the midst of more rapid restructuring than ever before.

The 1980s opened with interest rates at unprecedented levels. The real estate sector was, as a result, in recession. By mid-decade, sharply lower interest rates and sustained economic expansion led to explosive growth in mortgage financing. Home sales and resales were high; refinancings boomed; and commercial construction and financing set a record pace.

As the decade closed, the mortgage finance industry was retrenching from unsustainable record volume highs. Moreover, the thrift industry was undergoing a massive shakeout and regulatory reform.

The eighties also witnessed a near full maturation of the secondary mortgage market as the mainstream vehicle for financing mortgages. The separate functions of making, marketing, servicing, delivering and trading mortgages became increasingly "unbundled" and specialized in the hands of more narrowly focused firms. Securitization became the norm, not the exception. Global investor distribution networks became the watchword.

This article attempts to translate what's happening in these turbulent and exciting times into meaningful information to help mortgage finance executives plan for the future.

Specific forecasting may be reliable in predicting a future some three or even five years ahead. But beyond that, predictions quickly become meaningless. Really long-run forecasts become sidetracked or are made irrelevant by quantum changes in technology, in political and social affairs and in the rules of the game, all of which are inherently unpredictable.

So, we will merely lay out ranges of possibilities—describe what might happen, not what will happen. As Freeman J. Dyson, in his book *Infinite in All Directions* (Harper & Row, New York, 1987), says: "For the future beyond ten years ahead, science fiction is a more useful guide than forecasting. But science fiction does not pretend to predict. . . . It deals in possibilities, not in probabilities. And the most important developments of the future are usually missed both by the forecasters and by the fiction writers. Economic forecasting misses the real future because it has too short a range; fiction misses the future because it has too little imagination."

Further, the future is different things to different people. There are many things to know—and things cannot be known by a single method or judged by a single standard. The same facts can be arranged in more than one pattern, seen from several perspectives and displayed in many lights.

The mortgage market in recent years has been beset by high and volatile interest rates, the effects of deregulation, excess capacity, huge default and foreclosure losses, intense price competition and the evaporation of profits. There has been a shift from fixed-rate financing toward adjustable rate and other forms of "creative" financing. And there has been a sweeping trend toward securitization and increased reliance on the secondary market.

We recognize we now have a well-developed secondary market that assures the availability of mortgages in bad times as well as good. The secondary market, through Fannie Mae, Freddie Mac and Ginnie Mae, and through a number of private conduits, has proven a remarkably efficient engine for channeling capital for housing from the national and global credit markets into local housing markets.

The marvels of near instant worldwide communication and the ability to transform mortgages into a wide variety of rateable-tradable high-grade securities has made the mortgage market one of the most efficient and competitive marketplaces in existence. Housing consumers have been the beneficiaries. They can compete for housing finance on nearly equal

terms with giant corporations and obtain credit at rates only 150 basis points or so above the U.S. government's borrowing costs.

Yet, housing affordability has suffered even as the mortgage market has become more efficient. Home prices in much of the country have risen faster than incomes and faster than the CPI. Young people trying to buy their first home are most affected, as they struggle to accumulate a down payment and to command sufficient income to make a monthly mortgage payment that increasingly looms out of reach for more of them.

Among households headed by persons 25 to 34, the homeownership rate has dropped to about 45 percent, an eight percentage point drop from a decade earlier. The mortgage on a typical home in the late 1980s requires half again as much family income as it did two decades earlier.

The affordability crisis faced by renters is similarly distressing. Higher financing burdens and other costs of owning and operating rental housing have pulled rents up faster than the modest incomes of most renters.

As we look toward the future in our capitalist, free market society, the ultimate driving forces in the housing sector and elsewhere will remain profits and returns on investments. The future of real estate finance will be shaped by the combined forces of entrepreneurship, human ingenuity and technology. These forces will be at work armed with capital by those in pursuit of material gain but guided and restrained by public policy and regulation.

The way we finance housing and other real estate in the 21st century will almost certainly provide better mortgage products, more efficiently, at lower real costs. The competitive forces of the free marketplace work inexorably toward innovation and greater efficiency over the long term. Our business, like most, will do thousands of little things a little bit better, and once in a while a very few things a whole lot better.

Basic demand for mortgage finance

There will be a large and growing market for real estate finance, but it will be a leaner, less ebullient business than in the 1980s.

There will always be a need and therefore demand for housing, office and other commercial space, and for the financing of it. But the rate of growth in demand has reached a plateau and will even slacken a bit nationwide during the 1990s. Chart 1 shows net new household formations declining from an annual average of 1.6 million in the 1980s to 1.2 million in the 1990s. This will translate into an average annual need for some 1.4 million housing unit starts. That in turn suggests fewer new home sales and sharply lower multifamily construction.

Interestingly, existing home sales will rise gradually. Though the absolute number of additional new homes will be declining, the total stock of housing will be rising and so too will the number of existing units sold each year.

This less than roaring housing market and related employment and commercial activity will in turn generate only slowly growing and still cyclical needs for mortgage credit. We anticipate that home mortgage originations during the 1990s will average slightly more than $500 billion a year.

We expect loan servicing, by contrast, to continue growing. By the year 2000, home mortgage debt will likely reach $6 trillion. This is far more than double its level at the start of the 1990s. See Chart 2.

Demographics could play a beneficial role in lowering mortgage and other interest rates in the 1990s. As the bulge in the U.S. population grows older, it will shift over the next decade from credit-using, nonsaving young people to credit-supplying net savers.

This population shift almost certainly will be accompanied by diminished market share for first-time home

CHART 1. Housing Markets in the 1990s

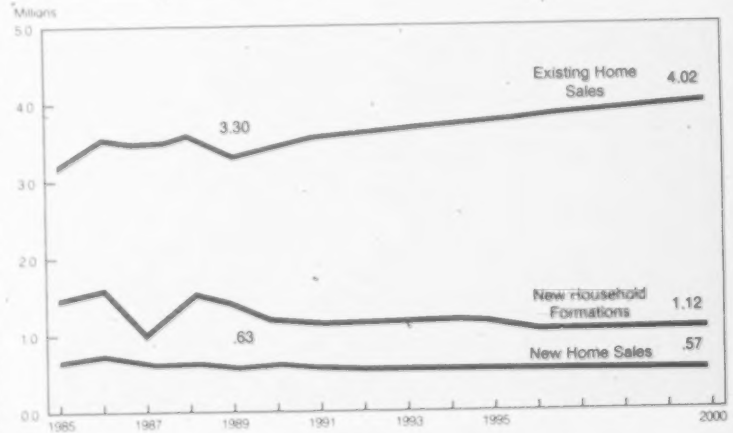
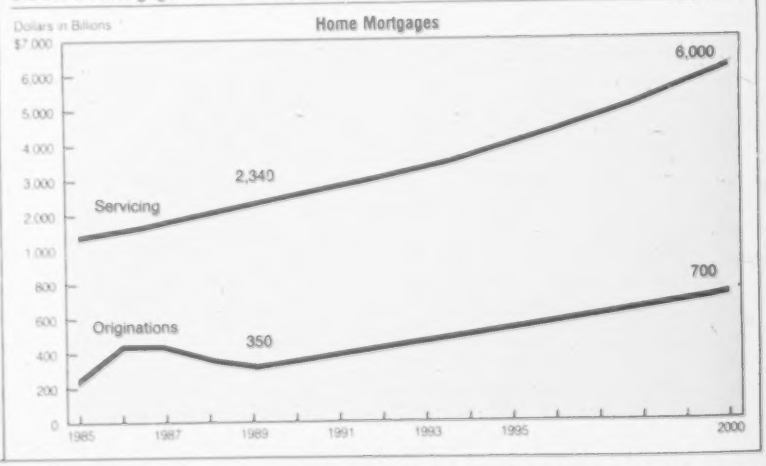


CHART 2. Mortgage Finance in the 1990s



buyers and the use of low down payment, conventional, FHA and VA mortgages. The move-up market for housing and mortgages will grow in importance, suggesting comparatively strong demand for high-balance, conventional, nonconforming financing.

Structure of the industry

Who will make, service and hold mortgage debt? As we enter the 1990s, the entire financial services and mortgage delivery system is going through a period of fundamental restructuring.

Consider first who will likely be the ultimate investors. Where will mortgage money come from? It used to be, at the beginning of the 1980s, that savings institutions and banks provided most of it. Indeed, the thrift industry alone held about half of all mortgage debt then. But as the decade ends, thrifts hold a much lower portion of the total, and their share is declining (Chart 3).

Meanwhile banks, pension and insurance funds and foreign institutions are becoming far more important as ultimate sources of mortgage funds. This trend will accelerate. Pension funds, without doubt, will grow in importance.

In terms of who will play what role in the mortgage market of the future, there is a paradox evolving. There is under way an homogenization of institutions on a global scale, but at the same time there is also a growing specialization of functions within firms.

In terms of who will play what role in the mortgage market of the future, there is a paradox evolving. There is under way an homogenization of institutions on a global scale, but at the same time there is also a growing specialization of functions within firms.

In the time-worn fashion of progressing through stages of specialization and division of labor, we envision the mortgage business becoming divided into separate, more efficient entities. The specialized business niches will be:

- Originating (or making) mortgages, including underwriting and quality control;
- Aggregating (or pooling) and warehousing mortgages, making them ready for delivery into the secondary market;
- Marketing and risk management prior to delivery to investors;
- Wholesale distribution to the investment community, and subsequent trading, along with the reconfiguration of cash flows into derivative products;
- Mortgage loan administration;
- Mortgage insurance and other credit enhancement functions;
- Holding mortgages and related securities as investors.

These functions will often be carried out within the same company, but need not be. Banks and thrifts that hold uninsured conventional loans in portfolio do all of these activities in-house. But low-cost/high-efficiency specialists will increasingly take on the individual functions.

The making and servicing of mortgages will continue to be the province of mortgage companies, banks and thrift institutions. Mortgage companies will prosper when they can take advantage of their total specialization in mortgages, their agility and their ingenuity as low-cost providers and servicers of mortgage products.

Thrifts and banks likely will converge and will fall into two, perhaps three, categories. Some will remain small scale, essentially consumer lenders. These will have a special role emphasizing mortgages in towns and communities where personal relationships remain important and price is not the determining factor.

At the extreme, some institutions will be so huge as to be almost impossible to define. Citicorp and American Express come to mind. They will have large market shares in the mortgage arena. Their success in the mortgage arena will be augmented by their name, scale and corporate presence; but a more vital question will be whether they can muster the ability to motivate and maintain entrepreneurial autonomy in a separate, mortgage-specialized subsidiary within the overall corporate structure.

Consider now the possibilities in the

CHART 3. Who Makes, Services and Holds Home Mortgage Debt? (Dollars in Billions)

	1980		1988	
	Amount	Percent	Amount	Percent
Mortgage Originations				
Thrifts	$ 66.5	49.7%	$ 186.2	49.7%
Mortgage companies	29.4	22.0	85.3	22.8
Commercial banks	28.8	21.5	95.5	25.5
All others	9.1	6.8	7.4	2.0
Total	$133.8	100.0%	$ 374.4	100.0%
Mortgage Servicing				
Thrifts	$482.0	50.4%	$ 823.8	38.9%
Mortgage companies	195.0	20.4	748.8	35.4
Commercial banks	179.1	18.7	402.2	19.0
All others	100.2	10.5	140.4	6.7
Total	$956.3	100.0%	$2,115.2	100.0%
Mortgage Holdings*				
Thrifts	$512.0	53.5%	$ 924.8	43.7%
Commercial banks	196.6	20.6	482.5	22.8
Pension and retirement funds	27.3	2.9	135.9	6.4
Federally chartered agencies	38.0	4.0	131.8	6.2
Insurance companies	28.2	2.9	143.0	6.8
All others	154.2	16.1	297.2	14.1
Total	$956.3	100.0%	$2,115.2	100.0%

* Including mortgage-backed securities

key traditional functions of mortgage finance—making, marketing and servicing mortgages.

The origination function

At no place in the mortgage market is the competition keener than in loan production. It will remain so. The business of producing mortgages will face the continuing challenges of: gaining efficient access to the consumer—the borrower—both directly and through real estate agents, while controlling costs and adapting automation and other new technology to speed and simplify mortgage lending.

Coupled with the ease of entry into the business and the tendency toward overcapacity, these forces will keep pressure on loan pricing for the foreseeable future.

The most successful firms in the 1980s were those that controlled costs most effectively. With demographics weakening and capacity excessive, intense price competition will mean that successful firms in the future will be leaner and even more tightly managed in the years ahead.

Economies of scale exist to a far lesser extent in loan production than in servicing. The annual volume of loan production needed to achieve profitability in a well-run firm will likely remain low. Indeed, diseconomies may set in above fairly modest production levels. So, relatively small, well-managed firms can prosper, particularly in so-called niche markets with niche products. Overall, there will be continuing moves toward reduced branch office overhead, "shirt-sleeve" rather than "managerial" employees, controls on excessive compensation packages, and consistently sound underwriting and systemwide quality controls.

The 1990s could well witness the emergence of the loan-originating correspondent firm, replacing the branch office network, as the predominant source of loan originations. Independent correspondents can be so efficient, move so fast, operate with such low overhead and enter or leave a volatile market so easily ("they pop up like mushrooms after a rainstorm") that they may render traditional branch offices obsolete in cost-price competitive markets. Risk management and quality control will be keys to long-term success among wholesale purchasers from such correspondents.

Intense price competition will mean that successful firms in the future will be leaner and even more tightly managed in the years ahead.

Expect in the decade ahead a trend toward the global standardization of mortgage products. Consumer desires and preferences all over the world are becoming more homogeneous.

The marketing function

At the heart of mortgage banking is the process of delivering, or marketing, mortgages into the secondary market. This function almost without doubt will become even more integral to the business of mortgage lending in the decade ahead.

And, central to the marketing function is maximizing profit in a framework of risk management. This will be as true in the future as in the past. We may not be able to forecast the level of interest rates, but we know they'll be volatile. It's a fact of life.

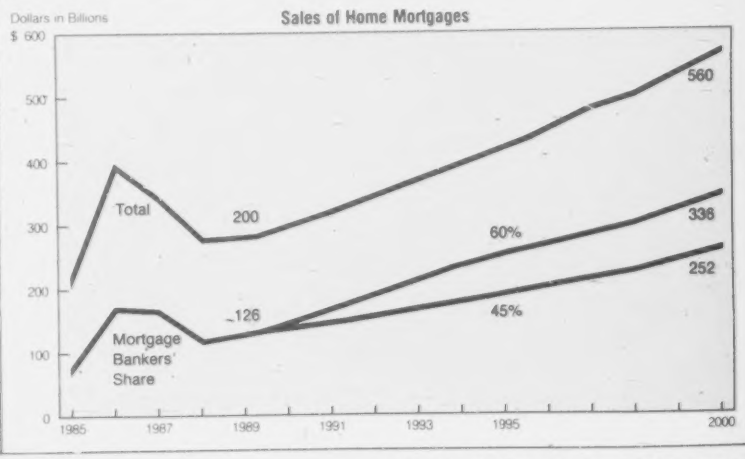
We can anticipate a continued search for better hedging vehicles and attempts to further shorten the period from loan application to delivery. There will almost certainly be advances in securitizing ARM loans, and these will become more readily accepted in the investor community. Other new products likely will involve securities with global appeal—for example, LIBOR-based floaters, with strip features and advances in reducing exchange rate risk.

While there well may be some further refinement in CMO structures, there is only a limited likelihood of any further quantum leaps in the technology of rearranging mortgage cash flows. Certainly the marketing function, more than any other part of the mortgage business, will be heavily dependent on computers, information processing and electronic communications. And it will be driven by intense competition based on price, not on personal relationships. This indeed may be the single biggest revolution over the past two decades in the way the mortgage business is conducted.

Loan originators and servicers will relate to the marketing function in different ways based mainly on their size. Small firms will deliver to wholesalers, which in turn will aggregate loans and perform most of the risk management and marketing functions.

The very largest servicers will increasingly issue REMICs directly, while most firms will continue to rely on the federal agencies and private

CHART 4. Secondary Market Activity in the 1990s



conduits for the securitization of their loans. Even the large private issuers will be constrained by the capacity of their corporate parents to carry the contingent liability of huge volumes of mortgage-backed securities.

The accompanying Chart 4 shows our projection that by the year 2000 home mortgage sales into the secondary market will reach about $560 billion. This will represent about 80 percent of loan originations. Mortgage bankers can be expected to be the principal players in delivering new mortgages into the secondary market. If they do no more than maintain their current market share of 45 percent, they will be selling more than $250 billion in loans by the beginning of the 21st century.

The servicing function

In loan administration, automation advances coupled with competitive forces will move the break-even level of real costs ever lower. The minimum volume of residential servicing needed to sustain profitability, probably in the range of 30,000 to 50,000 loans in the late 1980s, will continue to rise.

Hence the minimally optimal servicing operation will likely be far larger than the comparable scale of an efficient production operation. As a result, bulk servicing purchases will become a routine, institutionalized part of the mortgage business.

In servicing, the point where the most dramatic economies of scale were activated shifted from perhaps as low as 10,000 loans early in the decade to the 50,000 loan range late in the decade.

As direct servicing costs—people, data processing and the like—are brought down further, the 1990s will see a growing emphasis on controlling credit losses and contingent liabilities that are becoming more and more a part of the mortgage business.

Specialization

There probably is no one "ideal" mortgage firm. The consensus today is that small firms specializing in production have a viable place in the future. But to survive in the servicing business, you will have to be big and get bigger.

Midsize firms trying to perform as producers and servicers face a dilemma. They will be squeezed by the smaller producing firms' ability to contain costs and compete aggressively in local markets and by the economies of scale of larger servicers.

The future may see CEOs closer to, not further away from, the origination, servicing and administrative processes at both an operational and a leadership level.

These basic and differing economies of loan production and loan servicing point toward a continuing bifurcation of these two businesses. This prospect is heightened by tax and accounting rules. The ability to amortize purchased servicing, but not the servicing your firm originates, reduces current tax liabilities for firms that purchase servicing.

This strong combination of real economies plus tax incentives, if they continue, almost guarantees the continuance of huge amounts of servicing transfers. It also virtually assures the growth, further evolution and institutionalization of loan transfer mechanisms. This trend is reinforced by the fact that sales of servicing have become a tool to manage quarterly earnings.

To link separate production and servicing functions, correspondent-wholesaler networks have emerged. These networks have become an integral part of the engine that transforms highly differentiated individual mortgage products into homogeneous securitized investments.

Size of firms

While the smallest practical scale for a profitable servicing operation will continue to grow, the threshold of a successful loan administration department will remain low enough that there will be room for a good number of companies in the industry.

In a $6 trillion-plus servicing market, in which most economies of scale are achieved by the time you reach the $5 billion to $10 billion range, there is room theoretically for 100 or more major firms. That number grows if you believe that diseconomies set in at some point. "A penalty of size is that you try to do everything, and no one can do everything well," says Peter Drucker. Large companies emphasize quantity not quality, have costly extra layers of managements and respond slowly to changing market conditions.

In a global market, bigness could even be a handicap. Such a market demands features unrelated to bigness. It requires speed, agility and savvy. Even large firms can be expected to rely more on lean, decentralized decision making, small and flexible operating units and subcontracting.

Designing your firm's future

Tomorrow's executives face the ongoing challenges of developing and managing a product mix, a network for loan production and a distribution system. But also they must design, build and maintain their corporate entities—their concepts of organization suited to the business and competitive environment of the 1990s and beyond.

The marketplace and the consumers of our products will care not a whit how we structure ourselves. They are simply looking for a mortgage at the lowest cost with reasonably good service. Chief executive officers find themselves nonetheless in charge of firms and a seemingly incredible menu of possibilities as to their mission, core purposes and how to organize them.

The organizational concepts of business are changing. In the mortgage lending business as in much of American enterprise, the classical form of organizational structure with its layers and lines of authority may be obsolete. The future may see CEOs closer to, not further away from, the origination, servicing and administrative processes both at an operational and a leadership level.

The profit margins in each aspect of the business have been permanently reduced. We have seen beyond a doubt that the most successful firms are those that control costs at every stage of the business. Thus the focus of successful leadership will be on the per unit cost of producing the firm's total

TIMI[illegible]S EVERYTHING

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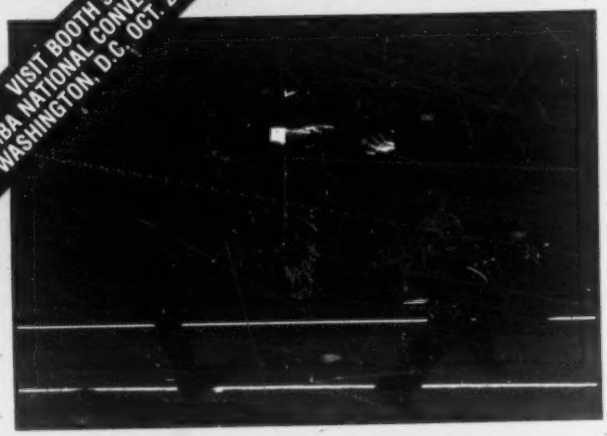

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How does one begin to plan for the future in such a rapidly changing world? Every company starts from where it is now. It starts with the hand it's been dealt: its size, capital, employees, location, product mix and customer base. Its business and political environment is essentially the same as everybody else's. The important and in fact essential first step in determining your own destiny is to have a plan—to know what it is you can do and want to do. As Lee Iacocca says, "The discipline of writing something down is the first step toward making it happen."

A plan begins with understanding the setting in which a firm finds itself, establishes a straightforward mission statement, which in turn is refined into specific long-term goals and shorter term activities with concrete objectives.

Probably the next most important step in designing your firm's future is to tell people about it. For an organization to function as a single, purposeful body, it needs an integrated planning-management system that everyone in the company understands.

In communicating or projecting the vision of one's firm, the top executive starts off with some very positive "givens." People in the mortgage business are in the housing and community-building business—serving basic human needs for shelter and decent surroundings. Unlike the uncertain need or demand for many other products, there will always be a genuine, fundamental need for housing and places to work, shop and play, and for the need to finance it.

Our industry is one of the most competitive in the world. So we are constantly forced to innovate and to deliver quality products at the lowest possible prices. We are a flexible, adaptive industry, nonunionized and, unlike much of the rest of American industry, relatively untouched by competition from abroad. These all are characteristics that will work in favor of our industry in meeting the challenges that lie ahead. **MB**

Warren Lasko is executive vice president of Mortgage Bankers Association of America.

With the troubles of 1987 more than just a vivid memory, many mortgage companies are still striving to improve productivity and contain costs. Over the past 1½ years the results of those efforts have been encouraging, but somewhat mixed. MBA's Ratio Analysis Survey (RAS) for the second quarter of 1989 indicates that servicing volume continues to rise while servicing expenses are moving downward. However, origination volume has been rather soft thus far this year, and costs remain stubbornly high. (The discussion that follows is based on data obtained from 18 companies that participated in the RAS in both the second quarter of 1988 and the second quarter of 1989.)

To achieve these belt-tightening objectives, many firms have consolidated their operations and introduced newly available technology into the workplace. A trend in loan production has been to close or merge origination offices and to further centralize underwriting and processing. In servicing, the focus has been on implementing cost-saving computer applications, as well as better loan quality control.

The most noticeable byproduct of these efforts has been the significant reduction in staffing levels at many mortgage companies. Between the second quarter of 1988 and the second quarter of 1989, the number of full-time equivalent employees fell by about 15 percent, or 45 employees per firm. The declines were widespread, with the number of origination employees falling by an average of 12 employees per firm, and the number of servicing employees dropping by an average of 8 employees per firm. Large staffing declines also occurred in areas other than origination and servicing.

In servicing, the mainstay of most mortgage companies, these decreases in employment have been the outgrowth of substantial increases in productivity. In fact, over the course of the year, the number of loans serviced per servicing employee jumped 23 percent, or 137 loans, from 587 loans in the second quarter of 1988 to 724 loans in the second quarter of 1989.

In turn, this rise in productivity has fostered a large drop in direct servicing costs. Although these costs remain quite high because of unusually large expenses for problem loans, servicing costs actually fell by 11 percent over the past year. At an annual rate, servicing expenses per-loan-serviced in the second quarter of 1988 were $103; by the second quarter of 1989, they were down to $91.

Data-processing costs associated with single-family servicing also dropped by 13 percent. At an annual rate, data-processing expenses per-loan-serviced were $9.48 in the second quarter of 1989. With servicing volume expected to continue rising, further gains in productivity could lower costs and improve profitability.

By contrast, direct origination costs per loan closed rose by 25.5 percent. Rising from $1,328 in the second quarter of 1988, these costs jumped to $1,666 in the second quarter of 1989. Even though origination staffs have been reduced, lending volume fell even more sharply during this period. Consequently, the number of loans closed per origination employee fell by 25 percent, from an annual rate of 36 loans in the second quarter of last year to an annual rate of 27 loans in the second quarter of this year.

The decline in lending volume noted in this survey is consistent with industrywide data showing that through May 1989, mortgage bankers' one- to four-unit lending volume was substantially lower than during the same period in 1988. However, with the earlier downward drift in mortgage rates expected to continue, mortgage bankers' lending volume should rise during the second half of the year.

On the whole, despite the rise in origination costs, two key measures of profitability showed marked improvement in the second quarter of 1989, relative to the same period last year. Return on average equity increased 58 percent to an annual rate of 8.20 percent, and return on average assets rose by 62.50 percent to an annual rate of 1.04 percent. While these figures are still below historical norms, the trend is clearly upward.

Data from the RAS is quite useful in tracking current developments in the mortgage banking industry. Additional member firms that would like to participate in this quarterly survey are welcome. Reporting is relatively easy, and the results are routinely distributed shortly after the end of each quarter via the ECHO system or in a typed report. For further information, contact Rick Murray, Programmer/Analyst, MBA Economics Department, at (202) 861-1941.

Mortgage Banking Industry Quarterly Productivity and Cost Ratios (18 Repeat Reporters)

	Second Quarter 1988	Second Quarter 1989	Percent Change
Productivity Measures:			
Single-Family Loans Closed Per Origination Employee	36*	27*	−25%
Single-Family Loans Serviced Per Servicing Employee	587	724	23%
Cost Measures:			
Direct Cost of Originating a Single-Family Loan	$1,328	$1,666	25%
Direct Cost of Servicing a Single-Family Loan	$102.52*	$90.92	−11%

* Annual Rate

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Economist
MBA Economics Department

VITAL STATISTICS

INTEREST RATES & YIELDS
1- TO 4-FAMILY MORTGAGES

1989	FHA OPINION SURVEY	FHLBB			FNMA		FHLMC	
	FHA New Homes[1]	CONVENTIONAL[2] FRM	CONVENTIONAL[2] ARM	Median Cost of Funds FSLIC Institutions	1-Yr. ARM	FRM Conv.	ARMs	FRMs
MAY	10.72%	11.14%	9.74%	7.99%	9.46%	10.55%	9.30%	10.77%
JUN	10.32	11.03	10.03	8.01	8.73	9.98	9.03	10.20
JUL	9.85	10.66	9.84	8.07	8.24	9.72	8.74	9.88
AUG	NA	10.33	9.57	NA	9.95	8.40	8.65	9.99

SELECTED SECURITIES

1989	FEDERAL FUNDS RATE	PRIME COMMERCIAL PAPER (3-Month)	U.S. GOVERNMENT 6-Month	1-Year	3-Year	10-Year	A-Rated Utility
MAY	9.81%	9.47%	8.41%	8.98%	8.98%	8.86%	10.09%
JUN	9.53	9.11	7.93	8.44	8.37	8.28	9.65
JUL	9.24	8.68	7.61	7.89	7.83	8.02	9.54
AUG	8.99	8.57	7.74	8.18	8.13	8.11	9.55

CURRENT SECONDARY MARKET YIELDS

SPREADS
(Basis Points)

1989	GNMA[3]	FNMA[3]	FHLMC[3]	GNMA Minus 10-Yr. Govt.	FNMA Minus 10-Yr. Govt.	FHLMC Minus 10-Yr. Govt.
MAY	10.29%	10.31%	10.30%	143	145	144
JUN	9.72	9.76	9.74	144	148	146
JUL	9.44	9.47	9.48	142	145	146
AUG	9.49	9.53	9.53	138	142	142

SECONDARY MARKET ACTIVITY
(Dollars in Millions)

1989	FNMA Portfolio Commitments	FNMA Portfolio Purchases	FNMA Mortgage-Backed Securities Outstanding	FNMA Mortgage-Backed Securities Issued	FHLMC Commitments To Sell	FHLMC Commitments To Buy	FHLMC Mortgages Purchased	FHLMC PCs Issued	GNMA Pass-Through Securities Applications	GNMA Pass-Through Securities Issued
APR	$1,118	$1,163	$191,420	$4,407	$5,945	$4,196	$5,861	$5,554	$3,513	$3,983
MAY	1,626	1,419	193,681	3,762	5,233	5,186	5,141	4,474	4,452	4,115
JUN	2,573	1,862	196,501	4,339	7,753	7,948	7,392	6,551	3,267	4,138
JUL	**2,513**	**2,091**	—	**5,464**	**5,934**	**6,609**	**5,720**	**5,180**	**4,395**	**4,895**
1988 TOTAL	23,435	23,110	—	54,878	41,271	70,669	44,075	39,777	58,578	56,531
1987 TOTAL	25,415	20,531	—	63,230	68,210	76,615	76,840	75,018	116,611	96,983
7 MONTH AVG. 1989	2,035	1,421	—	4,619	5,979	6,969	5,596	5,158	4,011	4,230
1988	2,368	2,221	—	4,198	2,826	5,369	3,148	2,702	4,341	4,279
1987	1,960	1,550	—	6,036	7,549	8,209	8,313	8,155	11,916	9,629

Housing Activity

Residential Structures

(Units in Thousands, Seasonally Adjusted Annual Rates)

	BY TYPE OF UNIT						BY REGION							
	HOUSING STARTS			BUILDING PERMITS			HOUSING STARTS				BUILDING PERMITS			
1989	Total	1-4 Units	5+ Units	Total	1-4 Units	5+ Units	Northeast	Midwest	South	West	Northeast	Midwest	South	West
MAY	1,308	1,019	289	1,347	970	377	176	244	513	375	179	245	528	395
JUN	1,406	1,027	379	1,308	940	368	168	242	552	444	177	234	506	391
JUL	1,424	1,086	338	1,281	979	302	195	267	532	430	160	232	478	411
AUG	**1,353**	**1,061**	**292**	**1,326**	**993**	**333**	**140**	**241**	**574**	**398**	**168**	**272**	**521**	**365**
1988 TOTAL	1,488	1,140	348	1,456	1,070	386	235	274	575	404	230	266	544	416
1987 TOTAL	1,621	1,212	409	1,535	1,114	421	269	298	634	420	272	282	575	406
8 MONTH AVG. (SAAR)														
1989	1,423	1,084	339	1,339	1,007	333	195	270	558	400	188	259	509	385
1988	1,473	1,134	338	1,427	1,063	363	259	274	562	384	252	263	529	383
1987	1,666	1,246	420	1,591	1,157	434	284	319	630	434	285	302	588	416

Home Sales

(Units in Thousands)

	EXISTING HOMES			NEW HOMES		
1989	Sold (SAAR)	Available for Sale	Months Supply At Current Sales Rate	Sold (SAAR)	Available for Sale	Months Supply At Current Sales Rate
APR	3,400	2,640	9.3	607	377	7.6
MAY	3,210	2,580	9.6	646	381	7.3
JUN	3,360	2,350	8.4	646	379	7.3
JUL	**3,400**	**2,320**	**8.2**	**739**	**371**	**6.1**
1988 TOTAL	3,594	---	---	676	---	---
1987 TOTAL	3,526	---	---	671	---	---
7 MONTH AVG. (SAAR)						
1989	3,400	---	---	645	---	---
1988	3,497	---	---	667	---	---
1987	3,614	---	---	695	---	---

Value of New Private Construction Put in Place

(Units in Billions of 1982 Dollars, Seasonally Adjusted Annual Rates)

	Total[a]	1-Unit	2+ Units	Nonresidential
APR	$280.0	$99.1	$21.5	$78.1
MAY	278.2	97.5	19.7	78.8
JUN	277.3	95.8	19.6	79.7
JUL	**277.1**	**95.4**	**19.1**	**80.2**
1988 TOTAL	281.8	103.5	19.3	77.9
1987 TOTAL	283.0	100.7	22.4	78.2
7 MONTH AVG. (SAAR)				
1989	280.8	100.0	19.9	80.3
1988	278.6	102.7	19.4	77.9
1987	280.9	99.4	23.2	76.4

LENDER ACTIVITY

LONG-TERM MORTGAGE LOANS CLOSED
By Type of Institution and By Type of Unit
(Dollars in Millions)

	1-4 UNITS					5+ UNITS					NONRESIDENTIAL				
	Total[a]	Mortgage Bankers	Savings & Loans[1]	Commercial Banks	Life Companies	Total[a]	Mortgage Bankers	Savings & Loans[1]	Commercial Banks	Life Companies	Total[a]	Mortgage Bankers	Savings & Loans[1]	Commercial Banks	Life Companies
1989															
FEB	$22,700	$4,494	$10,821	$7,029	$61	$2,616	$131	$1,361	$837	$67	$9,512	$38	$1,337	$6,884	$1,151
MAR	29,946	5,990	14,841	8,387	51	2,452	155	1,557	434	142	11,052	63	1,630	7,030	2,086
APR	27,890	5,530	13,233	8,730	85	2,480	331	1,206	366	221	8,917	122	1,340	5,216	2,104
MAY	**29,269**	**5,302**	**13,270**	**10,179**	**132**	**2,290**	**286**	**981**	**640**	**166**	**13,301**	**186**	**1,476**	**8,404**	**3,094**
1988–															
TOTAL	374,401	85,307	186,237	95,474	3,190	37,876	4,526	20,379	6,988	3,553	175,754	1,032	22,953	119,942	29,714
1987															
TOTAL	449,544	110,093	208,054	124,551	3,208	44,981	2,409	22,492	8,299	3,547	168,652	2,871	25,613	110,490	28,160
5 MONTH AVG.															
1989	27,099	5,320	12,896	8,403	80	2,554	293	1,307	530	185	10,641	106	1,476	7,006	1,916
1988	26,160	6,360	12,640	6,698	131	2,597	241	1,431	511	256	14,400	47	1,750	10,566	1,788
1987	41,062	12,040	17,231	11,225	304	4,242	188	1,691	870	236	11,899	357	1,876	7,823	1,764

MORTGAGE INSURANCE
(Units in Thousands, Dollars in Millions)

	APPLICATIONS RECEIVED (Units)				LOANS INSURED							
	TOTAL	FHA[6]	VA	PRIVATE	TOTAL		FHA		VA		PRIVATE	
					Units	Amount	Units	Amount	Units	Amount	Units	Amount
1989												
APR	135	76	15	44	91	$6,974	49	$3,064	15	$1,127	27	$2,783
MAY	149	91	15	43	93	7,109	50	3,167	15	1,164	28	2,778
JUN	157	96	15	46	107	8,155	60	3,774	14	1,072	33	3,309
JUL	**153**	**92**	**14**	**47**	**94**	**7,411**	**48**	**3,060**	**13**	**985**	**33**	**3,366**
1988 TOTAL	1,755	949	211	595	1,331	98,012	699	42,577	211	15,771	424	39,664
1987 TOTAL	2,340	1,211	408	721	2,282	159,668	1,320	81,881	451	33,312	511	44,475
7 MONTH AVG.												
1989	137	81	15	41	99	7,466	56	3,484	15	1,168	28	2,814
1988	153	85	16	52	109	7,909	57	3,453	17	1,246	35	3,210
1987	238	131	41	66	212	14,706	124	7,701	44	3,204	44	3,801

NA—Not Available; SAAR—Seasonally Adjusted Annual Rate

[1]Secondary market gross yields. Numbers shown for each month are the average of yields from the first day of the month shown and the first day of the subsequent month.

[2]Effective rate on loans closed.

[3]Securities for 0 to 30 day delivery.

[4]In addition to the categories of private construction shown, the total also includes these categories: residential improvements, railroads, electric light and power, gas, telephone and telegraph, petroleum pipelines, and farm nonresidential.

[5]In addition to the categories shown, the total also includes private pension funds, private MBS conduits, state and local retirement funds, Federal credit agencies, mortgage pools, and state and local investment agencies.

[7]Savings & Loans and Mutual Savings Banks.

[6]FHA applications received includes the Direct Endorsement Program.